Response to PhonepayPlus 'Business Plan & Budget 2015/16' Consultation

on behalf of The Number UK Ltd (118 118)

28 January 2015

Introduction

The Number UK ("TNUK") believes that PPP manages its budget efficiently and continues to do a good job in difficult financial circumstances. The continuing decline in the PRS market is not necessarily matched by an equivalent decline in the risk of consumer harm or in the workload of PPP more generally. Yet, it does place an increasing pressure on PPP's budget as it is required to do more (or at least the equivalent) for less.

PPP should therefore be congratulated on achieving a 25% real terms reduction in its budget since 2010, without any significant impact on its output or effectiveness. Industry should be grateful that PPP's efficient financial management has allowed it to maintain the levy at a broadly equivalent level, despite the significant decline in the revenues upon which the levy is calculated.

PPP will be acutely aware that its task is not set to get any easier. It notes a further 14.4% year on year decline, which is continuing into this year. Although PPP highlights some areas of the phone paid market which it believes could expand, it is very difficult to believe that the market will grow overall in the short-term. Further decline appears to be inevitable before perhaps seeing a levelling-off of a much smaller PRS market than has traditionally existed in the UK.

Owing to the ever increasing competition from different payment mechanisms (not to mention free services) it may be that that the PRS market (as defined by the Communications Act 2003) never again returns to its current level, let alone the level at which it existed 5 to 10 years ago. TNUK recognises (as must the rest of industry) that there is a limit to how far the PPP budget can be cut, without affecting its operational effectiveness.

When we reach the point at which the budget cannot be cut any further, but revenues continue to decline, the only option will be an increase in the industry levy. That will prompt a much closer examination of how PPP allocates its budget, as providers begin to feel the real impact of having to make increased contributions out of decreasing revenues.

TNUK believes that PPP will therefore need to review is spending in a far more fundamental manner than it has appeared willing to do to date. In essence, PPP exists in order to address consumer harm, which has been caused by providers in the PRS industry. As industry contributions increase, it therefore appears inevitable that it will come under pressure to ensure that it is <u>those</u> providers who pay for the costs which they cause to be incurred. This will require a far more precise degree of cost allocation and hypothecation than has previously existed, if PPP is to maintain the confidence of an increasingly declining, but also demanding industry. TNUK proposes that that process begins now.

PPP's insistence on retaining the current outdated funding model is based on its assumption that 'the money will always be there'. It assumes that phone paid services will continue to be provided in the same way in which they always have been and that it will always be able to claim its share through the flat-rate levy. But in reality, business models are changing faster than PPP may recognise and services that are currently subject to the levy may not be so for much longer. If PPP does not change its approach to funding increasingly out of pocket.

Polluter Pays

PPP's informal definition of 'polluter' has always been to include only those providers who have breached the Code of Practice. It has therefore sought to ensure that where it is required to take action against those providers, they pay a reasonable contribution towards the costs incurred in doing so, although for some reason PPP has never required that they fully cover those costs.
However, TNUK believes that the term 'polluter pays' is unhelpful because it unduly restricts the category of providers who may be expected to make an increased contribution towards PPP's costs. As PPP's spending comes under increasing scrutiny, this narrow definition of 'polluter' will no longer suffice, as it assumes that all other providers are equally responsible for generating PPP's workload, which is very far from the reality. PPP will have to be much clearer as to the areas of PRS on which it is spending its time and therefore by extension, which parts of the industry are causing it to incur costs. Providers who do not operate in those sectors are unlikely to accept an increase in their levy contributions to fund work, for which they are in no way responsible.

For example, '*Enforcement – Complaint Resolution*', '*Enforcement – Investigations*', '*Consumer Support*' and '*Industry Support*' together amount to nearly 80% of PPP's entire budget. Yet by their very nature, the need for work in this area has been generated by issues that have arisen in particular sectors and indeed, most likely, the activities of specific providers.

Whilst noting that PPP will recover some (but apparently not all) of the costs that it incurs in its investigations activity through its administration charge and fine income, that still leaves 50% of its budget being spent on sector specific activity, which only has relevance (and benefits) to limited parts of the PRS industry. PPP may believe that 'polluter' is the wrong word in this context, but whatever word is used, it is clear that some providers and industry sectors cause this work to undertaken, whilst others do not.

PPP refers more than once to the fact that "*we have extended the time recording within the organisation so that we can understand where the time is being spent to ensure that we are efficient in our work and able to recoup all costs appropriately under the principle of polluter pays*". The same comment was made in last year's Business Plan and Budget and yet it remains entirely unclear what this means in practice, how it is applied and particularly what purpose or benefit it serves. The levy is charged on a flat rate basis and unless a provider is subject to formal investigation, there is no means by which it can be required to make any further contribution.

TNUK believes that PPP must now fundamentally re-assess its resource allocation. It clearly has the tools to know precisely how it is spending its time, so it must now use those tools to implement a fairer funding mechanism. If it does not do so, but instead attempts to introduce across-the-board levy increases, as industry revenues decline, it will inevitably face opposition and complaint from those who become increasingly resentful at funding solutions to problems caused by others.

PPP must surely recognise that it is simply not sustainable to maintain a model of resource allocation and funding, which was created at a time when the industry was in a very different position and now appears increasingly outmoded. Again, we congratulate PPP on the reductions in budget which it has been able to make. But they cannot continue much further and therefore it must now move on to the next phase of re-assessing how it can financially sustain itself in the future in an era when resources will inevitably be tighter and much more searching questions will be asked as to how and why money is being spent.

The Funding Model

TNUK has raised concerns about PPP's funding model in response to both the Business Plan & Budget 2013/14 and the Business Plan & Budget 2014/15, as well as other related consultations and at meetings with the Executive. We regret that PPP has dismissed our arguments on each occasion simply by refusing even to engage in the debate, rather than by explaining the error of what we are saying or why it disagrees from a policy perspective.

We regret in particular that the current consultation contains no mention of the subject, as PPP appears to have 'moved on' from even requesting views as to the appropriateness of the model. TNUK believes that such an approach fundamentally misunderstands the nature of the argument and how it is likely to develop. We have explained above that as PRS revenues decline and budget cuts reach their limit, the issue of the levy will become more, not less important, as providers are expected to make increased contributions. PPP will be under ever increasing scrutiny as to how it spends its money by those who want to ensure that they are being asked to pay no more than their fair share.

TNUK fully expects that PPP's response will be the same as it has always been and that it will once again dismiss our concerns and refuse even to consider amending its funding model in line with the recommendations of its previously commissioned review. Nevertheless, we feel obliged to continue to reiterate our objections, such that they are formally recorded for any future action.

Our concerns centre on the fact that PPP continues to ignore the very clear recommendations of its own independently commissioned review conducted by KPMG. The KPMG review recommended switching to a service based funding model which would "*vary the levy between a small number of service segments which each display different risk characteristics (such as "high" or "low" risk in the first instance)*". The consequence of this change would be "r*evising levy calculations to more closely reflect the costs and benefits of Strategy and Policy work and the differences in the risk profile of certain services based on their track record or potential to generate consumer harm."* We are also deeply concerned that PPP has misrepresented the nature of KPMG's recommendations.

Furthermore, we object to the fact that PPP has always attempted to engender opposition to any changes to the funding model by asking industry whether it is prepared to contribute resources towards a further review, rather than acknowledging the reality that a review had in fact already been conducted and no additional industry contribution was required simply in order to implement its recommendations. We have also objected to PPP's negative bias by which it has made no reference to the positive benefits which a fairer and more equitable funding model would generate.

TNUK continues to believe that PPP's reference to a 'lack of consensus for change' as the only justification for not changing the funding model constitutes a very poor response from a regulator, who cannot possibly act only where there is agreement and consensus for it to do so, from those whom it regulates. It often repeats the erroneous statement that further funding would be required to engage external consultants to conduct a review of the funding model, when in reality an independent consultants' review has already been conducted and PPP simply chose to ignore its findings and recommendations. Rather than requiring

additional funding, PPP has wasted the money already spent on the KPMG review by completely disregarding it.
PPP also often repeats its peculiar justification that a funding review cannot take place unless there is a "*consensus*" or an "*appetite*" for it, which clearly ignores the obvious point that those who currently benefit from the unfair funding model in place will never have an "*appetite*" for it to change in a way which would financially disadvantage them. It further ignores the fact that there is no consensus in favour of the current funding model and therefore no reason why it should remain in place.

Although we will not repeat the detail of arguments made in response to earlier consultations, for the avoidance of any doubt, we entirely stand by the points which we have previously made and we regret that PPP has been unable to provide any meaningful response to them.

All queries in relation to this response should be to Simon Grossman, Director of Government, Regulatory & Business Affairs, The Number, Whitfield Court, 30-32 Whitfield Street, London W1T 2RG – simon.grossman@118118.com – 07971 050 001